

FRESNO COUNTY ASSESSMENT PRACTICES SURVEY AND ASSESSOR'S RESPONSE

OCTOBER 1999

CALIFORNIA STATE BOARD OF EQUALIZATION

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FOREWORD

The county assessor is responsible for the assessment of all taxable property within the county, except state-assessed property. The assessor's responsibilities include such things as: (1) discovering and taking inventory of all property within the county; (2) determining a property's eligibility for a full or partial exemption from assessment; (3) determining the proper assessee; (4) determining the location for assessment purposes of the property; and (5) determining the taxable value of the property in accordance with California property tax law.

Determining taxable value is usually the most difficult and subjective of the assessor's duties. In addition to the inherently subjective nature of the appraisal process, the assessor also has to determine whether the taxable value is to be based on current fair market value or on a restricted value. When there is construction activity on a property, the assessor has to determine whether the construction is to be assessed or whether it is excluded from assessment under the law. When there is an ownership transaction, the assessor has to determine whether the law requires a reassessment of the property or whether the property must continue to be assessed according to the existing value base.

The factors discussed above, as well as others not mentioned here, contribute to making local property tax assessment a difficult tax program to administer. It is also a very important program since the property tax is one of the most important sources of revenue for local governments and public schools. For property owners it is a major annual tax burden, and, since it is normally paid in one or two large installments rather than many small increments, it tends to be more visible than most other taxes. Accordingly, proper administration of the property tax assessment program is vitally important both to the public agencies that rely on the tax and to the people who have to pay the tax.

Although the primary responsibility for local property tax assessment is a function of county government, the State Board of Equalization has a number of duties in the property tax field imposed by the State Constitution and the Legislature. One of these duties, performed by the Board's County Property Tax Division (CPTD), is to conduct periodic surveys of local assessment practices and report the findings and recommendations that result from the survey.

Assessment practices surveys are required by Government Code sections 15640 et seq. These code sections require each county's assessment practices to be the subject of such a survey at five year intervals. The surveys must include research in the assessor's office to determine the adequacy of the procedures and practices employed by the assessor in the assessment of taxable property, compliance with state law and regulations, and other required duties. The surveys may include a sampling of assessments from the local assessment roll to determine eligibility for the cost reimbursement authorized by Revenue and Taxation Code section 75.60.

The assessor was provided a draft of this report and given an opportunity to file a written response to the recommendations and other findings contained in the report. This report, the county assessor's response, and the Board's comments regarding the response constitute the final survey report which is distributed to the Governor, the Attorney General, both houses of the State Legislature; and the county's Board of Supervisors, Grand Jury, and Assessment Appeals Board.

Field work for this office survey report of the Fresno County Assessor's Office was completed by CPTD staff from November 1997 through January 1998. This report does not reflect changes implemented by the assessor after the field work was completed.

The county assessor, the Honorable William C. Greenwood, and his staff gave us their complete cooperation during the assessment practices survey. We gratefully acknowledge their patience and good spirit during the interruption of their normal work routine.

Charles Knudsen, Chief
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October 1999

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EXECUTIVE SUMMARY

INTRODUCTION

Regardless of the size of the county, the assessment of property for tax purposes is a formidable task. Proper administration of this task is vital both to government agencies in Fresno County and to taxpayers. Because the job is so important and so complex, it is necessary for an independent agency such as the State Board of Equalization (BOE) to make periodic review of the assessor's operation. This survey report is the result of such a review of the Fresno County Assessor's Office by the BOE's County Property Tax Division (CPTD).

Government Code section 15640, in part, mandates that the State Board of Equalization shall:

(a)...make surveys in each county and city and county to determine the adequacy of the procedures and practices employed by the county assessor in the valuation of property for the purposes of taxation and in the performance generally of the duties enjoined upon him or her. (c) The survey may include a sampling of assessments from the local assessment rolls sufficient in size and dispersion to insure an adequate representation therein of the several classes of property throughout the county. (f) The board shall develop procedures to carry out its duties under this section after consultation with the California Assessors' Association. The board shall also provide a right to each county assessor to appeal to the board appraisals made within his or her county where differences have not been resolved before completion of a field review and shall adopt procedures to implement the appeal process.

It is apparent from this language that the Legislature envisioned the BOE's office research and appraisal sampling to be parts of a single, connected process, i.e., the evaluation of how well the county assessor is carrying out his or her sworn duty to properly assess all taxable property on the local tax roll. This evaluation was to be based on office research, or in certain circumstances, office research and actual field appraisals of sampled roll items. The way in which the office research and the sampling process is carried out was developed after consultation with the county assessors by the staff of the BOE's Property Taxes Department.

This survey was conducted according to the method mandated by Government Code section 15642. Following legislative direction, our survey primarily emphasizes issues that involve revenue generation or statutory mandate. This report is the culmination of a review of the Fresno County Assessor's operation that consisted of the CPTD's office research that examined current practices and procedures in key areas to see whether significant problems exist in the assessor's operation. Finally, the survey report offers positive courses of action, presented here as recommendations and suggestions, to help the assessor resolve problems identified in the program. The recommendations and suggestions contained in this report are based on our analysis of data which indicates that statutory violations, under or over assessments, or unacceptable appraisal practices may be occurring in specific areas.

Revenue and Taxation Code section 75.60 requires that the BOE certify a county as eligible for the recovery of costs associated with administering supplemental assessments. In order for a county to qualify as an eligible county, it must achieve an average assessment level that is not less than 95 percent of the amount required by law as determined by the BOE through its assessment-sampling program. In addition, for sampling for the 1996-97 fiscal year and subsequent fiscal years, the sum of the absolute values of the differences cannot exceed 7.5 percent of the legally required amount.

Based upon our assessment sampling for the 1992-93 assessment roll, the BOE certified Fresno County as an eligible county. This indicates that its assessment program was in substantial compliance with the law as of that sampling. Section 75.60 requires that certification remain in effect until the next sampling. Counties in which a survey has been conducted without sampling are subject to sampling if the BOE believes significant assessment problems as defined in BOE Rule 371 exist. The survey found no indication that significant assessment problems exist in Fresno County.

SUMMARY

During our previous survey of the Fresno County Assessor's Office, we concluded that both the real property and personal property assessments programs were essentially in proper order. Our review for this survey did little to change our opinion. However, our recommendations and suggestions reflect that some improvements are needed.

We have upgraded several suggestions from our prior survey regarding California Land Conservation Act (CLCA) properties to recommendations. For example, we now recommend using a risk rate higher than one percent on irrigated properties (the assessor uses a one percent risk rate on all CLCA properties).

We repeat a number of recommendations from our prior survey for improving the possessory interest assessment program. These recommendations relate to the valuation of the possessory interests.

When valuing petroleum properties, the assessor needs to recognize abandonment expenses in the same year as the economic limit of the property. The assessor's method overstates the market value of the property. In addition, the assessor should stop adding the present value of the abandonment expenses to the sale price when the sale price is used to determine the base year value of a property.

Other recommendations for improving the assessments of the personal property program include proper valuation of boats, assessment of certain supplies used by cable television companies, assessment of computers using the BOE's recommended value factors, and improvements to administrative policies. We also recommend the assessor stop assessing equipment in licensed vehicles.

We commend the assessor for being innovative in his handling of an ever-increasing assessment workload with stable staffing. To accomplish this, the assessor has computerized many assessment functions, saving thousands of work-hours. Future computerization projects will further facilitate the staff's work. Many of these computer projects will be financed through the use of funds furnished by the State-County Property Tax Administration Program.

RECOMMENDATIONS AND SUGGESTIONS

This report contains both recommendations and suggestions for improvements to the operation of the Fresno County Assessor's Office. Government Code section 15645 requires the assessor to respond in writing to the formal recommendations contained in this report.¹ Our recommendations are reserved for situations where one or more of the following conditions exists:

- Existing assessment practices do not conform to state constitutional provisions, statutes, BOE regulations, or case law;
- Existing assessment practices result in property escaping assessment or generation of an incorrect amount of property tax revenue;
- Existing appraisal practices do not conform to Board-adopted appraisal methodologies.

Our suggestions are considered less formal than recommendations, and the assessor is not required to make any response to suggestions. Typically, suggestions are BOE staff opinions on ways the assessor can improve efficiency, product quality, or other matters that do not call for formal recommendations.

The following is a summary of the formal recommendations and suggestions contained in this report, arrayed in the order that they appear in the text. The page is noted where each recommendation and its supporting text may be found.

Recommendations:

RECOMMENDATION 1: Do not exempt low-value property from assessment unless the board of supervisors adopts a current low value exemption resolution. _____ 8

RECOMMENDATION 2: Comply with Revenue and Taxation Code section 533 when identifying escape assessments on the assessment roll. _____ 9

¹ Government Code section 15645 requires that: "...Within a year after receiving a copy of the final survey report, and annually thereafter, no later than the date on which the initial report was issued by the Board and until all issues are resolved, the assessor shall file with the board of supervisors a report, indicating the manner in which the assessor has implemented, intends to implement, or the reasons for not implementing the recommendations of the survey report, with copies of that response being sent to the Governor, the Attorney General, the State Board of Equalization, the Senate and Assembly and to the grand juries and assessment appeals boards of the counties to which they relate."

- RECOMMENDATION 3:** *Use the date of enrollment as the date escape assessments are added to the roll, not the date an audit is completed. _____ 10*
- RECOMMENDATION 4:** *Comply with Revenue and Taxation Code section 75.55(b) by not canceling small supplemental assessments without authorization from the board of supervisors. _____ 17*
- RECOMMENDATION 5:** *Improve the California Land Conservation Act (CLCA) assessment program by: (1) relating the risk component in the CLCA capitalization rate to water availability and (2) developing written CLCA assessment practices and procedures. _____ 19*
- RECOMMENDATION 6:** *Improve the possessory interest (PI) assessment program by: (1) using a reasonably anticipated term of possession; (2) adding the present worth of future contract rents to PI equity selling prices; (3) not discounting PI values for lack of liquidity; (4) increasing documentation of the PI assessment record; and (5) using BOE approved capitalization techniques when valuing PI's. _____ 21*
- RECOMMENDATION 7:** *Improve the assessment procedures for water company properties by: (1) increasing the discovery effort for assessable water company property and (2) using unitary valuation techniques to develop current market values of water company property ____ 24*
- RECOMMENDATION 8:** *Improve assessment procedures for petroleum properties by: (1) recognizing abandonment expenses the same year as the economic limit of the property; (2) correctly determining the base year value of a property; and (3) revising the letters that request information from owners. _____ 27*
- RECOMMENDATION 9:** *Appraise mineral properties as a unit. _____ 28*
- RECOMMENDATION 10:** *Improve the assessments of cable television systems by: (1) including anticipated rate increases in income projections when using a discounted cash flow capitalization technique; (2) auditing the income and expense data supplied by the taxpayer; (3) including pole make-ready costs when valuing the cable distribution system; and (4) assessing supplies being held for inclusion into house-drops. _____ 29*
- RECOMMENDATION 11:** *Improve the audit program by: (1) not netting multiple years' audit changes; (2) notifying the county auditor of audit findings that could result in offsetting tax refunds and liabilities; and (3) adopting a consistent policy for determination of the years to be audited. _____ 32*
- RECOMMENDATION 12:** *Comply with Revenue and Taxation Code section 443.1 by always returning duplicate property statements. _____ 34*

- RECOMMENDATION 13:** *Improve business property valuation by: (1) using the equipment index factors as recommended in Assessors' Handbook Section 581; and (2) using the BOE's recommended value factors to value computers.* _____ 35
- RECOMMENDATION 14:** *Stop assessing cellular telephones and two-way radios installed in licensed vehicles.* _____ 36
- RECOMMENDATION 15:** *Improve the boat assessment program by: (1) annually appraising pleasure boats at market value; (2) assessing boats valued over \$400; and (3) using the Board-approved Vessel Property Statement AH 576-D, when a penalty for failure to file the property statement is contemplated.* _____ 37
- RECOMMENDATION 16:** *Improve the aircraft assessment program by: (1) complying with the requirements of Rule 252(a) to list general aircraft values in a separate section of the roll; (2) verifying the 12 days of public display for aircraft granted the exemption for historical significance under section 220.5; and (3) including sales tax in the value of aircraft unless the aircraft qualifies for the sales tax exemption as a "common carrier".* _____ 39
- Suggestions:**
- SUGGESTION 1:** *Improve the administration of the racehorse tax program by establishing a procedure for documenting compliance with BOE Rule 1054(a)(2).* _____ 11
- SUGGESTION 2:** *Record all building permits on appraisal records.* _____ 13
- SUGGESTION 3:** *Initiate a program for spot-checking self-reported new construction costs.* _____ 14
- SUGGESTION 4:** *Improve the assessment program for properties with a taxable value that is less than factored base year value by: (1) increasing the documentation that supports the market value estimate and (2) maintaining a current factored base year value for those properties.* _____ 16
- SUGGESTION 5:** *Improve the assessment procedures for Timber Production Zone (TPZ) properties by inventorying these properties for existing compatible uses and including the value of those uses in the assessment.* _____ 26
- SUGGESTION 6:** *Use the BOE-prescribed version of Form AH 571 F-2.* _____ 42

ADMINISTRATION

OVERVIEW OF THE FRESNO COUNTY ASSESSMENT ROLL

Since 1985-86, the local assessment roll has increased 182 percent and the number of assessments has increased almost 6 percent, concurrent with a staffing reduction from 132 employees in fiscal year 1987 to 128 employees in fiscal year 1996.

<u>ROLL YEAR</u>	<u>NO. OF ASSESSMENTS</u>	<u>ASSESSED VALUES</u>
1985-86	222,725	\$16,668,260,000
1997-98	235,889	\$30,376,150,000

The increased workload was accommodated by implementation of computerization of the assessment processes with an essentially stable staff size. From the 1991 fiscal year through the 1995 fiscal year the assessor's budget increased approximately 7.67 percent

<u>Year</u>	<u>1991-92</u>	<u>1992-93</u>	<u>1993-94</u>	<u>1994-95</u>	<u>1995-96</u>
Budget \$	\$5,925,225	\$6,196,012	\$6,020,122	\$6,241,946	\$6,380,200
Budgeted Permanent Positions	130	130	130	128	128

STATE-COUNTY PROPERTY TAX ADMINISTRATION PROGRAM

Under the provisions of Revenue and Taxation Code section 95.31, Fresno County elected to participate in the State-County Property Tax Administration Program (PTAP). This program is basically a grant of state monies to individual counties for use in property tax administration. The county must enter into a contract with the California Department of Finance, whereby the county agrees to enhance the property tax program. Those monies cannot be used to supplant an assessor's budget; a base level of staffing and total funding must be maintained.

Fresno County applied for and received a loan in the amount of \$1,165,249 for fiscal year 1996-97. Fresno County's contract with the Department of Finance requires that loaned amounts be used to enhance its property tax administration system and to reduce the backlogs of change in ownership appraisals, declines in value appraisals, and assessment appeal cases. Achieving the agreed upon goals is considered repayment of the loan.

PTAP funds are allowing the assessor to participate, with the county auditor-controller, in the development of a new automated property tax information system that will interface the two departments. Part of the money will be used to automate many assessment functions that previously required “hands on” participation by appraisers, technicians, and clerks. The assessor’s goal is to reduce the backlog of assessment appeals by 500 during the 1997-98 fiscal year, reduce the properties with declines in value waiting to be reviewed (there are currently 31,000 properties involved in this review), and reappraise all backlogged change in ownership events, which numbered 667 at the time of the contract.

ASSESSMENT APPEALS

The assessment appeals function is required by article XIII, section 16, of the California Constitution, which provides that the Legislature shall determine the manner and procedure of assessment appeals. Revenue and Taxation Code sections 1601 through 1641.1 are the statutory provisions that govern county boards of supervisors in the appeals function. Government Code section 15606(c) directs the Board of Equalization to prescribe rules and regulations to govern local boards of equalization, and the Board has adopted sections 301 through 326 of Title 18 of the California Code of Regulations (Property Tax Rules 301 through 326) to regulate assessment appeals.

The assessor’s office and the appeals board must have a close working relationship in order to make the entire appeals process efficient, particularly in the areas of case scheduling and document processing. However, the statutory requirement for separation of the authority and responsibility of both agencies must be observed. We reviewed the activities of the assessor's office that relate to assessment appeals.

The number of assessment appeals has drastically increased during the recent California recession that resulted in the decline of real estate values. Most of the increase in filings is based on the claim that the market value of real property is lower than the factored base year value. An owner of property who believes that the property’s current market value is less than the factored base year value is likely to request that the assessor review the assessment. A review that does not satisfy the owner is likely to prompt an assessment appeal. The table below, which shows a steady increase in the number of appeals, summarizes the Fresno County appeals workloads for five years.

<u>Assessment Year</u>	<u>Appeals Filed</u>
1993-94	779
1994-95	999
1995-96	2,076
1996-97	1,832
1997-98	1,996

We were unable to attend an appeal hearing because there were only two hearings scheduled during our review and in both of those continuances were granted. However, when we reviewed

the assessor's procedures for processing appeals, we found them to be satisfactory and the overall program to be well administered.

LOW-VALUED PROPERTY EXEMPTION

Revenue and Taxation Code section 155.20 authorizes the county board of supervisors to enact a resolution exempting from property tax all real property with a base year value and all personal property with a full value so low that the total taxes, special assessments, and subventions would amount to less than the cost of assessing and collecting them. The Fresno County Board of Supervisors passed resolution #91-107 in March of 1991. The resolution ordered that, for the *next* succeeding fiscal year, all classes of real property and personal property within the County of Fresno, with a full cash value less than \$500, be exempt from taxation. (Emphasis added.) Clearly the resolution was valid for only one year.

RECOMMENDATION 1: Do not exempt low-value property from assessment unless the board of supervisors adopts a current low value exemption resolution.

In our 1992 assessment practices survey, we commented that the assessor should review the low value exemption program, update it for possible new value limitations, and ensure that it is currently authorized. The Fresno County Board of Supervisors has yet to adopt a succeeding resolution.

However, the assessor continues to exempt low-value property at varying levels of taxable value. For example, possessory interests (PI's) are only assessed if the total value of the PI meets or exceeds \$3,000. Interviews with appraisal staff indicate an unwritten policy of not enrolling new construction under \$1,000. In some instances the decision to exempt the property is made by the staff appraiser assigned to work the assessment.

Without a resolution, the assessor has no authority to exempt low-value property from assessment. We recommend the assessor assess all taxable property unless the board of supervisors adopts a resolution authorizing an exemption for low value property.

DISASTER RELIEF

Revenue and Taxation Code section 170 provides that a county board of supervisors may adopt an ordinance authorizing tax relief for the owner of any taxable property that suffers a loss in value exceeding \$5,000 through damage inflicted by a disaster, provided that the owner is not at fault. This section prescribes procedures for calculating reductions in taxable value, applying for tax relief for the current year's assessment, and enrolling the value of restored property.

In our last survey, we recommended that the assessor's office request that the county board of supervisors adopt a continuing ordinance that would enable the assessor to grant relief to

taxpayers whose property has suffered a loss in value due to a misfortune or calamity. Currently, the county does not have such an ordinance. On occasion, the county board of supervisors has passed individual ordinances for certain calamities such as earthquakes, freezes, etc. All of these ordinances were adopted for specific disasters and were terminated on a specified date following the disaster. The assessor took our prior recommendation under advisement and concluded that Fresno County's "present interpretation and practice better accommodates the spirit of Proposition 13 and supplemental assessments."

The assessor presently relies on Revenue and Taxation Code section 51(b) as his authority for assessment changes that result from disaster, misfortunes, or calamities. However, section 51(b) does not provide the same level of tax relief as an ordinance adopted pursuant to Revenue and Taxation Code section 170. Even though the Revenue and Taxation Code makes adoption of disaster relief ordinances a local option, we encourage the assessor to again review the public policy benefits of a continuing disaster relief ordinance.

ASSESSMENT ROLL PROCEDURES

Roll changes allow the assessor to change assessed values after the assessment roll has been turned over to the county auditor. After the roll is delivered to the auditor, the change may be made, with a few exceptions, any time within four years of the making of the assessment that is being corrected. Roll changes are authorized for a variety of reasons by Revenue and Taxation Code sections 51.5, 531, 4831, and 4831.5. The most typical types of roll changes result from escaped new construction, clerical errors, and a current market value that is less than factored base year value. Fresno County processed approximately 8,000 secured roll changes for the 1996-97 tax year.

Identification of Escape Assessments

Revenue and Taxation Code section 533 specifies the language required to identify escape assessments on the assessment roll. If the escape assessment is entered on a roll which is not the roll for the assessment year in which the property escaped assessment, then the entry must be followed with the caption: "Escaped assessment for year 19__ pursuant to sections____ of the Revenue and Taxation Code." Both the secured and unsecured assessment rolls must contain these required captions exactly, as stated in section 533.

RECOMMENDATION 2: Comply with Revenue and Taxation Code section 533 when identifying escape assessments on the assessment roll.

The assessor uses a caption similar to that required by section 533 for secured escape assessments, but uses a significantly different caption for unsecured escape assessments. While the escape assessment captions are clear to the assessor's staff, the captions being used on both the secured and unsecured assessment rolls do not conform to those required by section 533. We recommend that the assessor comply with Revenue and Taxation Code section 533 when identifying escape assessments.

Interest Calculation on Escape Assessments

An escape assessment is an assessment that was not on the assessment roll when the roll was delivered to the auditor. An escape assessment must be added to the assessment roll, upon discovery, within the statute of limitations specified in Revenue and Taxation Code section 532. Certain types of escape assessments require that the interest described in Revenue and Taxation Code section 506 be levied on the amount of additional tax. Those situations are: (1) failure to file a required property statement (sections 501 and 531); (2) failure to report the cost of personal property accurately where the assessor has required a detailed statement from the assessee (section 531.3); (3) failure to file an accurate report on a BOE prescribed property statement (section 531.4); and (4) willful evasion as described in Revenue and Taxation Code sections 502 and 503.

Section 506 requires that the interest be calculated from the date(s) the taxes would have become delinquent, if they had been timely assessed, to the date(s) the additional assessment is added to the assessment roll. The escape assessment is entered on the roll when the information is committed to the roll process, not when an audit is completed.

RECOMMENDATION 3: Use the date of enrollment as the date escape assessments are added to the roll, not the date an audit is completed.

We found the assessor properly indicates whether interest is to be charged on the additional tax. However, the office procedure is to use the date an audit is completed as the date the escape is added to the roll. This date is often months prior to the audit even being approved by a supervisor.

Interest should accrue until the escape assessment has actually been added to the assessment roll. We recommend that the assessor stop using the date an audit is completed as the date of enrollment.

ANNUAL RACEHORSE TAX RETURNS

Since 1973 racehorses domiciled in California have been subject to an annual tax in lieu of the ad valorem property tax. The provisions of this tax are contained in Revenue and Taxation Code sections 5701 through 5790. Specific procedures and forms are prescribed by BOE Rules 1045 and 1046. BOE Rule 1045(a)(2) requires the assessor to furnish prescribed forms for the reporting of the in-lieu tax to persons believed to be liable for the tax and forms for reporting the names of persons whose racehorses are boarded with someone else. This rule also requires the assessor to retain a copy of all tax returns filed by taxpayers for a period of five years from the date the return becomes due. The rule also requires the assessor to notify the county tax collector of those persons to whom forms were sent. This notification must take place within ten days of the mailing of the tax forms.

In Fresno County annual racehorse tax return forms are timely mailed to the taxpayers. The record of persons believed to be liable for the annual racehorse tax to whom the assessor has furnished copies of forms is properly maintained; and copies of filed tax returns are retained as required by Property Tax Rule 1045(a)(2). However, implementation of the following suggestion would improve the administration of the racehorse program.

SUGGESTION 1: Improve the administration of the racehorse tax program by establishing a procedure for documenting compliance with BOE Rule 1054(a)(2).

We were not able to verify compliance with the statutory provisions regarding submission of the mailing record to the tax collector and receipt of paid returns. Property Tax Rule 1045 (a)(2) requires that the tax collector be given notice of those persons to whom the assessor has furnished copies of the annual racehorse tax return within ten days of the date the forms are furnished to taxpayers. Although the assessor's staff states that the notification is sent to the tax collector within a few days of mailing the returns, we were not able to verify the delivery date(s). An example of sufficient documentation would be to send a dated cover letter with the record of racehorse tax return mailings to the tax collector. We suggest that the assessor's staff establish a procedure for documenting compliance with the ten-day statutory requirement.

REAL PROPERTY VALUATION AND ASSESSMENT

BASE YEAR VALUES

Article XIII A of the California Constitution provides that the taxable value of real property shall not exceed its 1975 full cash value factored at no more than 2 percent per year for inflation unless there is a change in ownership or new construction. The 1975 full cash value and subsequent values that result from a change in ownership or new construction are known as base year values.

Change in Ownership (CIO)

Revenue and Taxation section 60 et seq. defines a change in ownership of real property for property tax purposes. Section 60 expresses the general concept that a change in ownership is an event that transfers, from one person to another, a present interest in real property with a value that is substantially equal to the value of the fee interest in the real property. The section also describes a present interest as including the beneficial use of the real property. Subsequent sections expand this definition for leased property and exclude certain types of transactions from the definition of a change in ownership. Board Rules 460 through 462.5 give additional instructions regarding determination of a change in ownership for property tax purposes.

Deeds and the recorded documents that transfer ownership of property are made available to the Fresno County Assessor's Office on 16mm microfilm approximately six workdays after deed recording. This microfilm and the Preliminary Change in Ownership Reports (PCOR's), filed by the purchaser at the time of deed recording, are received daily by the assessor's Assessment Services Division, Deeds and Transfers Section. The transfer section is responsible for verifying information on deeds and for determining the type of ownership change. The staffing consists of 15 office assistants and three supervisors; six of the office assistants are assigned to sales analysis work for the multiple regression appraisal activity.

The PCOR program seems to be very successful in Fresno County. We base this conclusion on the fact that the PCOR program is experiencing approximately an 80 percent compliance rate; the Change in Ownership Statement (COS) return rate is approximately 90 percent. This indicates that the assessor has knowledge of the sale conditions for approximately 98 percent of all change in ownership events.

Since 1989 the Fresno County Assessor's Office has developed base year values for certain single-family residential properties by use of an activity they refer to as direct enrollment. The assessor uses a computerized multiple regression analysis to confirm that a purchase price is market value. However, only approximately 60 percent of single family residential properties with change in ownership events are used in the database the assessor maintains for the multiple regression appraisal activity. The assessor indicates that the sales not used are those sales for which he is unable to confirm that the conditions of the sale met the conditions described in Revenue and Taxation Code section 110(a). However, given that the assessor has achieved a 98

percent level of compliance with PCOR/COS requests, information to make a determination that the sales met the section 110 requirements should be readily available.

Purchase prices are validated for direct enrollment according to the following criteria: (1) subject's purchase price is accepted as market value if purchase price is not less than 95 percent nor more than 105 percent of appraised value; (2) subject's purchase price is adjusted to appraised value if purchase price is not less than 90 percent nor more than 110 percent of appraised value; and (3) subject sale held for further review if value difference exceeds 10 percent. Even though, in this process, no consideration is given to the conditions for a market value transaction as expressed in Revenue and Taxation Code section 110(b), the sale price is used as the new base year value for 95 percent of residential changes in ownership.

We concluded from our review that, overall, the assessor's activities relating to change in ownership events effectively produce the results required by relevant law.

New Construction

Revenue and Taxation Code section 70 describes new construction as any event, occurring subsequent to the prior lien date, that is: (1) an addition to real property or (2) an alteration of real property constituting a major rehabilitation of the property or conversion of the property to a different use. In Fresno County, the primary method of discovering new construction is building permits issued by various government agencies. In addition, staff appraisers may discover construction activity while they are field canvassing their assigned areas or from the annual business property statement.

BUILDING PERMIT PROCESSING

There are 16 agencies that issue building permits in Fresno County. A member of the appraisal staff picks up permits for the County of Fresno twice a month. Permits in small towns are usually mailed in or brought in by an appraiser during the first week of every month, along with a list of permits that have had final inspections. Permits from the City of Fresno are provided to the assessor on a computer disk.

Two office assistants intensively screen building permits for assessment potential. The procedures and process that staff follows for assessing new construction are acceptable. However, we do have a concern regarding low cost permits, because discarded permits are not documented on the assessment records.

SUGGESTION 2: Record all building permits on appraisal records.

It is the assessor's policy to disregard permits with a value less than \$1,000. Unless a permit has an indicated value of \$1,000 or more, generally it is not cycled into the permit processing system, nor is it recorded on the assessment record. Many of these permits are for non-assessable construction; however, discarding them precludes an appraiser from checking the extent of the construction that, on review, could be found to be assessable. The building permit estimated

values might be erroneous and understated; also an accumulation of low-valued new construction on a single property could result in assessable new construction.

Most permit information is useful to an appraiser, whether or not it involves assessable new construction. Permit data can provide a property's history of alterations and additions. A permit history helps an appraiser determine whether or not a property should be reappraised. Permit data furnishes valuable points of reference (e. g., building activity date and description of construction) for validating the accessibility of structural costs reported by taxpayers on Schedule B of the Business Property Statement.

We suggest that all building permits be recorded on individual appraisal records.

SELF-REPORTED NEW CONSTRUCTION

In Fresno County, approximately 40 percent of assessable new construction is valued based on taxpayer reported cost. Most properties and costs are not reviewed or spot-checked for accuracy, except for new residences and major new construction.

SUGGESTION 3: Initiate a program for spot-checking self-reported new construction costs.

Although we have no evidence of erroneous assessments due to lack of a review process or inaccurate reporting by property owners, our experience in other counties has shown random audits to be essential. We suggest the assessor implement a procedure to review a fixed percentage of self-reported new construction costs in order to verify the information received.

Tenant Improvements

Tenant improvements (TI's) are defined as additions to real property that are owned by the tenant. The assessor uses Form (FCA 2311), Appraisal Procedure Memorandum, for coordinating TI assessments between the real and personal property divisions. The assessor typically values tenant improvements using the taxpayer's reported costs, but cost data from Marshall Valuation Service may be used when reported costs are questionable or considered unreliable. Assessments for tenant improvements are processed in the following manner.

- The real property division discovers assessable TI's from building permits and from Schedule B of the Business Property Statement (BPS).
- New construction questionnaires are sent for TI costs and description.
- When a tenant vacates, the assessor does not reappraise the improvements unless additions have been made.

- All TI's are assessed to owner of the land and building except for those in a community shopping center, a regional (by county's definition) shopping center, and those in shopping centers that have a supermarket. Tenant improvements for these properties are assessed as Trade Fixtures (TFI) on the unsecured roll.

A portion of the BOE-prescribed Business Property Statement (Schedule B of Form 571-L) is reserved for the reporting of costs expended by tenants for improvements to rented premises (land and buildings). Such property may be trade fixtures. Trade fixtures are real property items installed by a tenant that, by agreement between a landlord and a tenant, remain the property of the tenant. The Civil Code would characterize such property items as the personal property of the tenant. However, this contract is not the determining factor for determination of the property's classification between real property (fixture) and personal property for property tax purposes. BOE Rule 122.5 (d) instructs assessors not to consider the contract as representative of the intent of the parties, but instead rely upon the outward appearance of the property.

If the personal property division receives reported costs on the BPS (Schedule B) for TI's that are determined to be a real property item, a copy of the BPS is forwarded to the real property division for review and action. If the real property division discovers *trade fixtures* that are determined to be personal property, the information is forwarded to the personal property division for assessment.

We randomly selected and reviewed assessment records of properties on the assessor's 1996 "K-List" for shopping center properties and Business Property Statements with TI's. We reviewed the records for: (1) proper reported cost and description, (2) proper identification and classification of TI's by the personal property division, and (3) proper coordination between the personal property and real property divisions.

The majority of the BPS's we reviewed lacked descriptions of reported structure costs that would be adequate for determination of taxable new construction. Reported structure costs on the BPS should be carefully analyzed before they are used as a basis in valuing the property. The assessor's present procedure for referring these costs to the real property division should accomplish the required analysis. In general, we found the assessor's staff to be efficient and thorough in their assessment of tenant improvements with good coordination between the real and personal property divisions.

DECLINES IN VALUE

The California Constitution, article XIII A and Revenue and Taxation Code section 51 require that real property subject to article XIII A be annually assessed at the lower of the base year value, adjusted annually for inflation, or the current market value, as defined in Revenue and Taxation Code section 110. Adverse economic conditions during the early 1990's have caused the market value of real property in many areas of California to be less than their inflation adjusted base year value, also known as factored base year value (FBYV). As a result, many

county assessors have had to make taxable value reductions in unprecedented numbers. The Fresno County Assessor has been no exception. As part of our survey of the Fresno County Assessor's Office, we examined the assessor's program for discovering market values that are less than FBV. The assessor became aware of market values that were less than FBV as early as the mid-1980's. Due to the prevailing economic conditions in Fresno County, the current market value does not exceed FBV for many properties. The number of properties with a market value less than FBV has increased more than 500 percent between the 1993 and the 1997 lien dates. The annual increase is shown in the following chart.

<u>Roll Year</u>	<u>Number of properties with taxable (market) value less than factored base year value</u>
1993/94	7,893
1994/95	14,502
1995/96	19,634
1996/97	23,902
1997/98	41,764

Except for homogeneous single family residential housing tracts, Fresno County lacks written procedures for identifying properties that have market values less than FBV. For properties in homogeneous single family residential housing tracts, the assessor utilizes a computerized linear regression analysis process for discovering and valuing such properties. All other properties are handled individually by the appraiser responsible for the geographic area in which the properties are located. In these areas, values are not as easily determined as those for properties found in homogeneous areas. The methods for discovery are: (1) knowledge of an area's value; (2) specific requests for review by individual taxpayers; and (3) formal appeals to the assessment appeals board. Whether the property is valued by the linear regression program or valued individually, the assessor attempts to annually review all properties with a taxable value less than FBV.

To determine the quality of the assessor's program, we randomly selected and reviewed assessments in this category. The results of our examination revealed that overall the assessor is effectively accomplishing the legal requirements for recognizing and valuing properties that have experienced declines in value. However, there are areas that require improvement.

SUGGESTION 4: Improve the assessment program for properties with a taxable value that is less than factored base year value by: (1) increasing the documentation that supports the market value estimate and (2) maintaining a current factored base year value for those properties.

Sixty-five percent of the assessments reviewed, with a taxable value less than FBV, lacked any reference to comparable sales data. In these instances the appraisal records indicated only an estimated market value. No reference was made as to how the estimate was obtained. Supporting documentation for an assessment that is less than FBV should be increased. We also found property with a taxable value less than FBV, and with a completed new construction event, that did not have the base year value of the new construction included in the 1997 FBV maintained on the computerized assessment record. Without an accurate factored base year value, it is

impossible to determine a correct taxable value. Factored base year values should be kept current for all properties.

SUPPLEMENTAL ASSESSMENTS

Revenue and Taxation Code sections 75 through 75.80 describe the process for making supplemental assessments. A supplemental assessment is made to reflect the difference between a new taxable value resulting from creation of a new base year value and the taxable value that exists on the current roll. If the change in ownership occurs between the lien date and the end of the current fiscal year, an additional supplemental assessment is required to reflect the difference between the new base year value and the taxable value on the roll being prepared.

In Fresno County the supplemental assessment process begins with the initial action by the appraiser, who indicates the new value on the appraisal record. The appraisal record is transferred to the technical support unit, where values are analyzed and transcribed onto the front sheet of the appraisal record. The record is then sent to the real property support unit, where the values are entered into the supplemental assessment program of the mainframe computer system. The computer program can calculate and prorate most supplemental assessments. Difficult assessments, such as fractional changes in ownership, are returned to an assessment technician, who manually calculates each supplemental assessed value and forwards them to the real property support unit for entry into the computer system.

Supplemental assessment notices are automatically printed the day following entry into the computer system and are reviewed by the appraisal support staff prior to mailing to the taxpayer. Two notices for each assessment are printed, one for the taxpayer and one for the assessment file.

Our review of the supplemental assessment program indicated that, overall, supplemental assessments are being processed timely and accurately. However, we do have a recommendation for improving the program.

Revenue and Taxation Code section 75.41(d) allows the county auditor to cancel any supplemental tax if the total tax due is \$20 or less. Section 75.55(b) allows the board of supervisors to adopt a resolution authorizing the assessor to cancel any supplemental assessment where the resulting taxes would be \$20 or less, and supplemental assessments on manufactured home accessories where the taxes would be \$50 or less.

RECOMMENDATION 4: *Comply with Revenue and Taxation Code section 75.55(b) by not canceling small supplemental assessments without authorization from the board of supervisors.*

The assessor occasionally cancels some small supplemental assessments that generate tax bills under \$10.00. Without the board of supervisors' resolution authorized by Revenue and Taxation Code section 75.55(b), the assessor has no authority to cancel any supplemental assessments. We recommend the assessor stop canceling small supplemental assessments.

SPECIAL PROPERTY TYPES AND PROCEDURES

CALIFORNIA LAND CONSERVATION ACT PROPERTY

An agricultural preserve is established between a land owner and the county or city pursuant to the California Land Conservation Act of 1965 (CLCA). Lands under contract are valued for property tax purposes on the basis of agricultural income-producing ability, including any compatible use income (hunting, communication facilities, etc.). Revenue and Taxation Code sections 422 through 430.5 deal explicitly with the valuation of property subject to agricultural preserve contracts. They are assessed at the lowest of this agricultural value, the current market value, or the factored base year value, as defined in article XIII A of the California Constitution.

In Fresno County, properties restricted by a CLCA contract are utilized as irrigated cropland, vineyards, orchards, grazing, and dry farm land. For the 1997 lien date, Fresno County had 1,590,245 acres in 14,679 parcels encumbered by 6,999 CLCA contracts. During the period of January 1996 through November 1997, the CLCA contracts for 31 parcels were canceled and the CLCA contracts for 174 parcels were placed in a non-renewal status.

The calculations for the taxable value of properties restricted by a CLCA contract are computerized, including the annual recalculation of non-renewal values and the comparison between the CLCA restricted value and factored base year value. Our review of computer-generated land and living improvement CLCA values indicate that the assessor's computerized program is performing appropriately.

Our 1992 assessment practices survey had two suggestions regarding CLCA properties. One suggestion dealt with the use of a standard risk rate of 1 percent for all CLCA assessments, regardless of the risk associated with the source of the income. The assessor continues this practice.

Our second suggestion addressed the periodic field review of all CLCA assessments and the proper classification, documentation, and assessment of all improvements that are under CLCA contract. These properties do not presently get an annual field review, although the majority are field checked more frequently than was the prior practice. We found that the assessor is in substantial compliance with this suggestion.

Our review indicates that overall the CLCA assessment program is good. However, there are still some areas that need improvement.

RECOMMENDATION 5: Improve the California Land Conservation Act (CLCA) assessment program by: (1) relating the risk component in the CLCA capitalization rate to water availability and (2) developing written CLCA assessment practices and procedures.

RISK COMPONENT IN THE CLCA CAPITALIZATION RATE

The income from dry farmed properties, grazing lands, and irrigated properties with an assured water supply has greater certainty of receipt than income from irrigated property with uncertain water supplies. Therefore, as discussed on page II-27 of Assessors' Handbook, Section 521, *Assessment of Agricultural and Open-Space Properties*, it would be appropriate to utilize a higher risk rate to value the income from irrigated agricultural properties with uncertain water supplies than using a standard risk rate on all CLCA restricted property. We recommend that the risk rate used to capitalize CLCA income into value be differentiated based on the need for water and the availability of water.

DEVELOP A WRITTEN SUMMARY OF CLCA ASSESSMENT PRACTICES AND PROCEDURES.

Although the present appraisal staff is very familiar with the assessment of CLCA properties, in the future, whoever is assigned to the program may not possess this first-hand knowledge. Currently, the only written guidance available are informal notes, which are not adequate should the current supervising appraiser and other staff appraisers not be available. In the best interests of program continuity and maintaining high assessment standards, we recommend that the assessor develop detailed written procedures for the assessment of CLCA properties.

TAXABLE GOVERNMENT-OWNED PROPERTY

The California Constitution exempts from taxation any property owned by a government agency that is located within the agency boundaries. Government-owned land and/or improvements located outside the agency's boundaries may be taxed if they were subject to taxation at the time of acquisition. These properties are commonly referred to as section 11 properties.

Until 1995, the provisions of article XIII A of the California Constitution were not applied to taxable government-owned real property. The California Supreme Court decided, in City and County of San Francisco v. County of San Mateo et al. (1995, 10 Cal.4th 554), that the real property limitations of article XIII A apply to taxable government-owned real property located in counties other than Inyo and Mono. The court determined that article XIII A did not exclude from its valuation limitations taxable property owned by local governments, and that both article XIII A and article XIII, section 11 could be applied to taxable government-owned real property.

In order to properly implement this decision, two factored base year value calculations should be maintained for each assessment of taxable government-owned land. These factored base year values are described in the California Constitution, article XIII A and article XIII, section 11. Each is an independent calculation representing a potential taxable value. Each has a different base year and a different factor that is applied to the different base year values. The taxable value for taxable government-owned land, located in other than Inyo and Mono Counties, should be

the lowest of: (1) the 1967 assessed value times the Phillips (Section 11) factor; (2) the current fair market value; or (3) the Article XIII A factored base year value.

Improvements are assessed if taxable when acquired or if they replace taxable improvements. The taxable value of improvements should be the lowest of: (1) the current full cash value; (2) the article XIII A factored base year value; or (3) the highest full value ever used for taxation of the improvements. Any new improvement, constructed by a government agency, that is not a replacement of a taxable improvement, is exempt from taxation.

We randomly selected and reviewed the records of 21 of the 93 section 11 properties on Fresno County's 1997-98 assessment roll. Our review indicates that the assessor's program for discovering and valuing this type of property results in assessments that comply with legal requirements.

POSSESSORY INTERESTS

A taxable possessory interest (PI) is a private person's right to use publicly owned real property for a term less than perpetuity. Revenue and Taxation Code sections 107, et seq., provide assessors with the fundamental instructions for these assessments. BOE Rules 20 through 28 provide clarification for the statutory instructions.

The Fresno County Assessor's program for discovering PI's includes an annual request to all governmental entities in the county for information on agreements with private parties. Staff appraisers annually contact approximately 100 public agencies by letter to request current information on new or changed tenancies or rents. When the information is returned, it is compared with the prior year's list to find deletions and assessable additions. If there are any changes, the new information is placed in the appraisal record folder and filed in the "Call Back" file for review.

Three supervising real property appraisers are responsible for the review and revaluation of PI assessments. However, the supervisor may delegate the activity to a subordinate. Fresno County's 1997-98 assessment roll contained 1,056 taxable PI's, with a total assessed value in excess of \$102 million.

In our previous survey of the Fresno County Assessor's Office, we recommended several changes be made to the county's PI assessment practices. Some of these recommendations have been implemented. Others, including estimates of the term of possession and valuation of PI rights subject to a change in ownership, have not. For this reason, some of the prior recommendations are being repeated. We also make new recommendations for improving PI assessments.

RECOMMENDATION 6: *Improve the possessory interest (PI) assessment program by: (1) using a reasonably anticipated term of possession; (2) adding the present worth of future contract rents to PI equity selling prices; (3) not discounting PI values for lack of liquidity; (4) increasing documentation of the PI assessment record; and (5) using BOE approved capitalization techniques when valuing PI's.*

REASONABLY ANTICIPATED TERM OF POSSESSION

When the purpose of an appraisal is to determine the market value of a PI, the term of possession must reflect the actions of the marketplace. After reviewing a number of PI appraisal records, we noted PI values were often based upon terms of possession that did not meet that test.

One example of this practice is the assessor's use of a three-year term of possession for airport hangars at the Reedley Airport when typical tenancies approximate ten years. An appropriate term of possession for Reedley Airport PI's would be ten years, the length of a typical hanger tenancy.

In another example, the gross annual rent paid by small concessions at the county fairgrounds was used as the concessions' PI value. Although the concession agreements are issued on a yearly basis, many concessionaires have enjoyed consecutive years of use. In this instance the term of possession estimated by the assessor is unclear, but it is highly unlikely that any estimate of a reasonably anticipated term of possession would result in a present value of the economic rent that is precisely the same amount as one year's gross rental fee. The value of a PI with a short contract term should be based upon a reasonably anticipated term of possession. For the PI's at the fairgrounds, the term should be estimated by measuring the number of years that the concessionaires typically conduct their business at the fairgrounds. An additional flaw with the assessor's use of gross rent as a PI value is discussed in a subsequent paragraph titled "Capitalization Techniques."

The term of possession is a difficult and critical component of the valuation procedure for PI's. When capitalizing a market rent into a PI value indicator, Property Tax Rule 23 requires the assessor to use the reasonably anticipated term of possession, whether the term is shorter or longer than specified in the written agreement. In order to determine a reasonably anticipated term of possession, the assessor should consider the history of the property's use, the intent of the public agency, sales prices, and the intent and actions of the possessor. We recommend that the assessor comply with the requirements of BOE Rule 23 when estimating the term of possession of a PI.

PRESENT WORTH OF UNPAID FUTURE CONTRACT RENTS

The assessor has assessed several PI cabin sites located on lands owned by of the U. S. Forest Service. These assessments consist of privately-owned cabins built on government-owned sites. These cabins, along with the leasehold interest in the site, can be sold in the same manner as other property. However, the fee interest in the site remains the property of the government.

We found that when these types of properties are sold, only the purchase price of the equity was enrolled as the total PI value. This method does not recognize all of the PI value in the land. The purchaser paid the seller for the equity (the improvement and the leasehold interest) and also assumed the contract rent obligation. The amount paid for the improvement and leasehold interest does not include the additional value recognized by the buyer's assumption of the contract rent obligation, which is analogous to assumption of a debt.

When a cabin experiences a change in ownership, Revenue and Taxation Code Section 110 and BOE Rules 2 and 25(a) require the assessor to determine the base year value of the possessory interest by adding the present worth of the future contract rents to the sale price of the owner's equity in the PI. We recommend that the assessor include the present worth of any contract rent obligations assumed by the buyer in the base year value of a PI.

DISCOUNTS FOR LACK OF LIQUIDITY

A taxable PI value represents the present value of the permitted use. In conceptual terms, it is the lump-sum amount a new tenant would pay in advance to the owner of the fee, without additional payments being due, for the permitted use, with the lessee being responsible for all expenses of operating the property.

We found several PI assessments with values that were discounted 5 percent for a lack of liquidity (i.e., the calculated PI value was reduced by 5 percent because of a perceived difficulty in the lessee's ability to sell the equity in the PI). This is an inappropriate valuation technique. The value the assessor is seeking is that value described in the previous paragraph, not the *price* that someone who is contemplating selling the equity might receive. Once calculated, the value indicator should not be further discounted.

DOCUMENTATION

Many of the PI files we reviewed lacked lease data, permits, or other documents that were the basis for the creation of the PI. Additionally, in many PI files we were unable to find any remarks stating what term, rate, or income the staff appraiser used to calculate the PI value.

Documentation is an important, necessary first step in valuing the PI. Without such documentation, it can be difficult to determine the commencement of occupancy, the reasonable term of possession, the economic rent, the date of a change in ownership, ownership of improvements upon termination of the tenancy, and other facts essential to making a valid PI appraisal. Lease data is also needed to properly schedule reappraisal activity resulting from a future change in ownership. At a minimum, we recommend that each PI assessment file contain the economic rent, capitalization rate, contract rent, and term of possession used to calculate the PI value. If the PI value is a function of a direct sales comparison valuation technique, the equity sale price and sales comparison analysis should also be included.

CAPITALIZATION TECHNIQUES

The assessor uses annual gross rent for the PI value of concessions at the county fairgrounds. The chief appraiser stated that, in his opinion, this is a reasonable method for estimating value.

This is a reasonable method only if the reasonably anticipated term of possession is one year, and no operating expenses are necessary for the production of the income; or if the gross income multiplier is the capitalization technique. The issue of an appropriate term of possession is discussed in previous paragraphs. There was no documentation in the file indicating that the *lessees* paid all operating expenses. There also was no documentation that indicated gross income multipliers had been derived from sales of comparable PI's.

The failure to properly process gross income into an amount of income appropriate for capitalizing into a value is a significant deviation from BOE approved valuation techniques, as is the failure to properly derive income multipliers. BOE Rule 8 describes the requirements for proper calculation of capitalized income values. We recommend that the assessor require his staff to comply with BOE Rule 8 when valuing PI's.

WATER COMPANY PROPERTY

Assessable water company property may be owned by "municipal" systems located on taxable government-owned land or private water companies. The California Public Utilities Commission (CPUC) may regulate private water companies. Private water companies that are not regulated by the CPUC consist of mutual water associations and small companies that are exempt from CPUC jurisdiction. Each type presents different appraisal issues.

The California Constitution, article XIII, section 3(b) exempts from taxation property owned by a local government within the government's boundaries. This exemption includes property owned by city water departments or water districts. When the water system is located outside of the government agency's boundaries, this exemption does not apply. In those instances, article XIII, section 11 requires that publicly owned water system property, located outside the agency's boundaries, be taxed if it was taxable at the time it was acquired by the city or district. We found that property owned by the municipal water systems, located within agencies' boundaries, was correctly exempted from taxation. Municipal water system property, located outside of the agencies' boundaries, was also assessed correctly.

A mutual water company is a private association created for the purpose of providing water, at cost, to be used by its stockholders or members. The association, when incorporated, can enter into contracts, incur obligations, own property, and issue stock. However, if not incorporated, it can only do these things in the names of all its members. Corporations organized for mutual purposes are not subject to regulation by the California Public Utility Commission, unless they deliver water for compensation to persons other than stockholders and members.

We found six mutual water companies in Fresno County. Because of a lack of documentation in the assessment records, we were not able to determine whether or not these water companies' assessed values were correct.

To determine if the assessor has assessed all the water company property in Fresno County, we obtained a listing of all water supply sources annually inspected by the Fresno County Division of Environmental Health, the state's Office of Drinking Water, and the CPUC. The

Environmental Health Division list contained 406 water sources. Some of these properties are not assessed. Because of a lack of documentation in the assessment records, we were not able to determine if any of the property is escaping assessment.

RECOMMENDATION 7: Improve the assessment procedures for water company properties by: (1) increasing the discovery effort for assessable water company property and (2) using unitary valuation techniques to develop current market values of water company property

DISCOVERY OF ASSESSABLE PROPERTY

The assessor's staff is uncertain how many municipally owned (inside or outside the municipality's boundaries), mutually owned, or privately owned water systems exist within Fresno County. A November 3, 1997 list, generated by the assessor's office, contains the names of 23 water system companies with a total of 55 land parcels assessed. There is no program for assessing water system property other than that of the four private, regulated water companies. Consequently, some water system properties may have escaped assessment. Research is needed to determine what property is owned by which company and the assessment status of the property.

We recommend that the assessor periodically contact the Fresno County Department of Public Health, Division of Environmental Health and the state's Drinking Water Field Operations Branch to obtain updated lists of tested water supply sources. The CPUC can furnish a list of regulated water companies doing business in Fresno County. Once this information is obtained, the assessor's staff should confirm that the assessment status of the properties described on the list is consistent with the requirements of property tax law.

Our review of the assessor's water company listing revealed that the only annual CPUC reports and business property statements the assessor receives are those provided by the four known private, regulated water companies. There are 406 water sources on Fresno County's Environmental Health System "Water System Inventory" list, dated December 8, 1997. Each private water system that owns these water sources should be required to file an annual business property statement.

If the water system is regulated by the CPUC, the assessor should also obtain a copy of the system's annual CPUC report. In addition, the assessor should require that all private water systems submit copies of their articles of incorporation and by-laws. These articles will assist the assessor in the proper classification of each water company.

As previously mentioned, there are 406 properties listed by the Fresno County Environmental Health Department as municipally, mutually, or privately owned water systems in Fresno County. We recommend that the assessor investigate the status of these water systems and assess them if assessable and not currently properly assessed.

For each private water company the assessor should obtain: (1) articles of incorporation with amendments; (2) bylaws with amendments; (3) list of lands, improvements and water distribution systems owned, with location and identity of each item; (4) proof of ownership of land and improvements in the company's name; and (5) a list of all assessor's parcels served by each private water company. When this information is obtained, the assessor can better ensure the proper assessment of each private water company.

VALUATION TECHNIQUES

Some water companies are operated for profit. Some of these are subject to economic and service level regulation by the California Public Utilities Commission (CPUC). Real property owned by these water companies is subject to the valuation limits of article XIII A. However, because of CPUC economic regulation, the current market value of real property owned by these water companies is likely to be less than FBYV. This occurs as a result of CPUC tariff requirements that are a function of the acquisition cost of the property, less regulatory depreciation. This is exactly opposite from the calculation of FBYV, which is the result of an acquisition value increased by an annual statutory inflation amount. Therefore, it is necessary to annually determine the taxable value, as of the lien date, by comparing current market value to the FBYV.

In Fresno County there are four water companies subject to CPUC regulation. The assessor's personal property division annually receives property statements and CPUC reports, which are reviewed for assessable property. Intermittently, the assessor determines market values for the real property owned by these companies by adjusting only the land value (i.e., the lower of current market or the factored base year value of land is used as the land's taxable value). The improvements' taxable value is based on FBYV.

This is an inappropriate method of determining the market value of a regulated water company's property. Regulated water company property should have a value calculated on a unitary basis, taking into consideration any CPUC restrictions on earnings, with the resulting unitary value allocated to the various assessments.

Unregulated water companies are similar to regulated water companies in that they are operated for profit. Our survey determined that the assessor is aware of 12 unregulated private water companies. The assessor determines the taxable value of the property of these companies in a manner similar to that used for regulated water companies. The preferred valuation technique is the same as that described above for regulated water company property, except there is no economic regulation by the CPUC to consider. It is important to understand that the lack of CPUC economic regulation precludes use of Historical Cost Less Depreciation (which is usually a surrogate for the CPUC rate base) as a value indicator.

TIMBERLAND

Land that has been zoned Timberland Production Zone (TPZ) is subject to assessment in accordance with the special TPZ site classifications that exclude the value of the standing timber. In Fresno County there are 21 parcels of TPZ land totaling 1,506 acres. Our review found that,

overall the assessor is appropriately assessing TPZ lands. However, our review found one area where the assessment of TPZ parcels might be improved.

Revenue and Taxation Code section 435(a) requires the assessor to include in the value of each TPZ parcel, the appropriate site value described in section 434.5, plus the value, if any, attributable to existing, compatible, nonexclusive uses of the land. These uses result from leases, permits, or other agreements the landowner may have with other parties, allowing the timberlands to be used for purposes other than the growing, harvesting, or storing of timber.

SUGGESTION 5: Improve the assessment procedures for Timber Production Zone (TPZ) properties by inventorying these properties for existing compatible uses and including the value of those uses in the assessment.

Our review of the TPZ appraisal records indicated that the assessor included compatible use values in some TPZ assessments. These compatible use improvements and sites are accurately recorded on the assessment record, assessed values are appropriate, and applicable supplemental assessments are issued.

However, in Fresno County, once land is zoned TPZ and assessed as such, there is little contact between the assessor's office and owners of TPZ parcels. The assessor does not make inquiries about possible compatible uses that may exist on TPZ properties in Fresno County. Our review of the assessor's TPZ assessment records disclosed that, while permitted exclusive uses such as home sites, cabins, and hunting lodges are being assessed when discovered, there is no systematic canvassing of TPZ landowners to determine the existence of compatible uses. This creates a discovery problem if there is income to the TPZ property from existing compatible uses.

The assessor could easily remedy this situation by periodically requesting information on compatible uses from the TPZ landowners. Any such uses should be assessed in addition to the restricted TPZ site values. We suggest that the assessor contact TPZ landowners in Fresno County for information on compatible uses.

MINERAL PROPERTY

Petroleum Property

Fresno County employs a mineral consultant to value petroleum properties. An appraisal assistant processes the paper work associated with the annual production reports and other filings by the taxpayers.

RECOMMENDATION 8: *Improve assessment procedures for petroleum properties by: (1) recognizing abandonment expenses the same year as the economic limit of the property; (2) correctly determining the base year value of a property; and (3) revising the letters that request information from owners.*

ABANDONMENT EXPENSES

The current practice of the assessor and his consultant is to account for abandonment expenses two years after the economic limit of a property has been reached. This assumes that payment of those costs is from a source of funds other than cash flow from the property. This practice is contrary to the recommended procedure found in Chapter 8 of Assessors' Handbook section 566, *Assessment of Petroleum Properties*.

The correct procedure recognizes the abandonment expenses the same year that the property reaches its economic limit, or allows an annual allocation from the cash flow sufficient to satisfy the abandonment expense requirements (i.e., a sinking fund). Postponing the abandonment expenses in the cash flow reduces the present value of those expenses and overstates the market value estimate of the property. We recommend the assessor use valuation procedures that are consistent with Board approved procedures.

BASE YEAR VALUE

For petroleum properties that have recently sold, the assessor calculates base year value by adding the present value of the abandonment expenses to the sale price. We believe this practice overstates the base year value of the property.

In effect, the assessor is making a cash equivalent adjustment to the sale price. Appropriate cash equivalent adjustments are described in BOE Rule 4(a) and 4(b). Abandonment expenses are operating expenses that have a negative effect on the value that is reflected in the sale price. Abandonment expenses are not an assumed debt, described in BOE Rule 4(b), which should be added to sale price. We recommend the assessor not add the present value of the abandonment expenses to the sale price of a petroleum property.

LETTERS

The assessor and his consultant have developed a "request for information" letter which is sent to owners of petroleum property. The letter asks for copies of work papers that contain data which might be useful for developing appraisal parameters for petroleum properties. If no response is received, a second request is sent stating that failure to comply with the request will result in the taxpayer's property being reassessed under Revenue and Taxation Code section 501, and that penalties might be applied.

Revenue and Taxation Code section 441(d) provides that the taxpayer must make the material available for examination. Revenue and Taxation Code section 470(a) provides that the taxpayer must provide true copies of the requested data. To encourage cooperation, the assessor might consider citing Revenue and Taxation Code section 462, which provides that a person is guilty of

a misdemeanor if, after a written request from the assessor, he or she refuses to make available information that is required by Revenue and Taxation Code section 441(d).

However, the penalties cited can only be assessed when a taxpayer fails to file a State Board of Equalization prescribed property statement. This request for information letter is not a BOE prescribed property statement. We recommend the assessor stop informing taxpayers that failure to comply with an information request may subject them to a penal assessment.

Sand and Gravel Property

The assessor's real property division staff has been appraising the sand and gravel properties in Fresno County. However, beginning with the 1998 assessment year, these properties will be appraised by a mineral appraisal consultant.

The assessor's staff has been valuing the mineral rights separately from the plant and equipment associated with those properties. The "royalty method" is used to value the mineral rights. The current market values of the mineral rights and the plant and equipment are then compared to their adjusted base year values to determine the taxable value.

RECOMMENDATION 9: Appraise mineral properties as a unit.

The assessor's valuation technique is not correct because it fails to find the market value of the appraisal unit.² Property Tax Rule 469(e)(1)(C) requires that declines in the value of the mineral property be recognized when the market value of the appraisal unit, (i.e., land, improvements including fixtures, and reserves), is less than the adjusted base year value of the same unit. Failure to appraise the mineral property as a unit could result in the aggregate taxable value of the appraisal unit exceeding the value required by the law. We recommend that the proper appraisal unit be valued.

CABLE TELEVISION

The appraisal of a cable television (CATV) system encompasses many property classes and types. There are three appraisal units contained in such a system. Those units consist of: (1) land, including possessory interests in land, and structures, including head-end sites; (2) fixtures, including the cable distribution system; and (3) personal property, including converters, supplies, (held for replacements or for servicing new areas of the franchise), computers, office equipment, etc. Our discussion, recommendation, and suggestions are all made under this topic, even though they could be included in other topics contained in this survey report.

A recent sale of a major CATV property in Fresno prompted an appraisal of that property by the assessor. Our review of that appraisal revealed that the value was arrived at after considerable

² Leach pads, tailing facilities, and settling ponds are considered separate appraisal units when comparing current market value to a factored base year value.

fact gathering and investigation. However, the implementation of the following recommendations could improve the CATV appraisal.

RECOMMENDATION 10: Improve the assessments of cable television systems by: (1) including anticipated rate increases in income projections when using a discounted cash flow capitalization technique; (2) auditing the income and expense data supplied by the taxpayer; (3) including pole make-ready costs when valuing the cable distribution system; and (4) assessing supplies being held for inclusion into house-drops.

ANTICIPATED RATE INCREASES

The assessor's cash flow analysis used projected income data supplied by the taxpayer and increased that income by two percent to reflect subscriber growth. The assessor did not increase income for anticipated rate increases even though a 12.5 percent rate increase was scheduled for February 1997. We recommend the assessor include anticipated rate increases in the cash flow estimate.

AUDIT INCOME AND EXPENSE DATA

The assessor uses taxpayer-supplied income and expense data to arrive at a possessory interest value in land. This data has never been audited. We recommend the assessor verify the income and expense data.

POLE MAKE READY COST

When installing an aerial distribution network, CATV systems typically incur pole make-ready costs, also known as pole rearrangement costs. The owner capitalizes these expenditures in the system's financial records as part of the tangible property.

For the recent appraisal, the assessor did not include, in the system value, over \$3.7 million dollars in expenditures of this type, that the taxpayer had capitalized. An audit in 1996 revealed that the taxpayer had these expenditures capitalized as part of its distribution system costs. However, the audit findings did not include these costs in the value of the distribution system. A portion of the value of the property represented by these costs has escaped assessment. We recommend the assessor consider these costs when valuing the cable TV system.

SUPPLIES

Supplies are assessable unless they qualify for the business inventories exemption described by Revenue and Taxation Code section 219 and BOE Rule 133. Supplies for CATV house-drops, also known as connect-drops, include cable and electronics used to wire the interior and exterior of a subscriber's building, in order that the subscriber might receive service. The customer is not billed for time and materials for the connection, nor is there a lease agreement for leasing the connection. House-drops are analogous to a telephone line that carries signals to and from a residence.

The characterization, by members of the assessor's staff, that the supplies are exempt because they are business inventory, is not correct because the supplies are not held for sale or lease in the ordinary course of business. The assessor's staff also suggested that supplies being held for inclusion in house-drops should be exempt because a court decision, Tele-View Systems vs. County of Contra Costa, exempting house-drops. In fact, the court's decision did not exempt the house-drops but said that, once installed, the interior portion of the house-drop was a fixture and part of the real property to which service is provided. Since the CATV provider did not assert ownership, the interior portion of the house-drop is assessable to the owner of the served property. However, since the value added for each individual property is so minor, the assessor usually does not increase the property owner's assessment for this installation.

The assessor has erroneously allowed the business inventory exemption for supplies held for incorporation into house-drops. We recommend that the assessor assess these supplies.

PERSONAL PROPERTY VALUATION AND ASSESSMENT

INTRODUCTION

The Fresno County Assessor's personal property division consists of a chief auditor-appraiser, a supervising auditor-appraiser, 13 auditor-appraisers, 16 full-time assessment clerks, and two part-time assessment clerks. This staff is responsible for annually processing approximately 76,000 property statements and completing, on average, 650 audits.

In our prior survey, we made seven recommendations and two suggestions to bring the assessor into conformity with the law or audit and appraisal standards set forth by professional organizations. We found that three of the recommendations were either fully or partially implemented and that both suggestions have been implemented.

BUSINESS PERSONAL PROPERTY

Audit Program

The business property division is responsible for conducting property tax audits. Property tax audits are conducted approximately ten and a half months out of each year, and the remaining time is devoted to processing property statements. The staff (as mentioned in our prior two surveys) remains production oriented and has a high audit production record. To assist management, the division maintains detailed records on employees' production and other activities.

The personal property division staff is professional and well trained. The staff includes two certified public accountants (CPA's), four auditor-appraisers who have passed the CPA examination, and seven auditor-appraisers who hold an Advanced Appraiser Certificate issued by the Board of Equalization.

The main objective of the audit program is to ensure that all assessable property is properly reported on the annual business property statements. A good assessment program is built on the premise of complete and accurate reporting by all taxpayers, regardless of business type or size. Auditing all value levels of taxable property promotes compliance. It ensures that, regardless of property size, the taxpayer can be held accountable for proper reporting to the assessor.

Revenue and Taxation Code section 469 requires that all accounts with assessed values over \$300,000 be audited. Property Tax Rule 192 requires that the \$300,000 level be reached in each of four consecutive lien dates. We found that the majority of mandatory audits are completed prior to expiration of the statute of limitation. Waivers of the statute of limitation are obtained for those that will not be completed before the expiration of the statute. The audit program is well managed and efficient; fewer than ten waivers are required annually.

The assessor has averaged 659 audits annually for the time period beginning July 1, 1992 through June 30, 1997. Both mandatory and non-mandatory accounts are audited; approximately 75 percent of the audits result in assessment roll changes. The following is a summary of audit production and results for the five fiscal years ending June 30, 1993 through June 30, 1997. This audit activity resulted in a total increase in property tax revenue in excess of \$10 million.

Year Ending June	Total Audits Competed	Mandatory Audits Completed	Escapes	Refunds	Absolute Change (Escapes Plus Refunds)
1997	593	332	\$135,757,000	\$42,183,000	\$177,940,000
1996	709	354	\$188,805,000	\$40,735,000	\$229,540,000
1995	681	334	\$157,321,000	\$49,034,000	\$206,355,000
1994	724	330	\$142,689,000	\$45,527,000	\$188,216,000
1993	590	325	\$147,888,000	\$66,905,000	\$214,793,000

In our prior survey, we suggested that the assessor require documentation, in the audit narrative and/or work papers, that the taxpayer's compliance with Revenue and Taxation Code section 64(c) (change in ownership) was reviewed. The assessor has successfully implemented procedures for documenting the review for a change in ownership. In addition to indicating "yes, no, or non-applicable" for change in ownership on the audit checklist, copies of income tax returns, or notes as to their content, are included in the working papers.

Audits completed by the Fresno County Assessor's Office are well referenced and have adequate support for findings. The auditors reconcile costs reported on the property statement to supporting schedules and perform other tests of the financial records as necessary. Overall, the audit activities meet the standards expected for a property tax audit program. However, we do have recommendations for improving the audit program.

RECOMMENDATION 11: *Improve the audit program by: (1) not netting multiple years' audit changes; (2) notifying the county auditor of audit findings that could result in offsetting tax refunds and liabilities; and (3) adopting a consistent policy for determination of the years to be audited.*

MULTIPLE YEARS' AUDIT CHANGES

Revenue and Taxation Code section 531 requires that, if any property belonging on the local roll escapes assessment, the assessor shall enroll the property on discovery at its value on the lien date for the year in which it escaped assessment. When incorrect assessments are discovered as a result of an audit, Revenue and Taxation Code section 533 requires that **tax refunds** be an offset against proposed **tax liabilities**, including accumulated penalties and interest.

During an audit of four years' of a business's financial records, under-assessments (escapes) and over-assessments (refunds) are often discovered. The assessor, in some instances, offsets under-assessments of one year against over-assessments of another year (i.e. audit results are netted). If the net difference is considered immaterial, it is not enrolled. The assessor has no written policy regarding when an offset is appropriate; the decision is at the discretion of the individual auditor. This has resulted in a variety of situations in which offsets are made. All offsets are inappropriate assessment practice unless the offsets are in the same assessment year, and the property is situated in the same tax rate area.

There is no statutory provision that authorizes offsetting (netting) over-assessments and under-assessments of different assessment years, only for an offset of *tax refunds* against *tax liabilities* from different tax years. Tax rates can vary from year to year; penalties and interest on escapes need to be calculated before any offsetting takes place. These calculations are the county auditor's responsibility, not the assessor's.

The assessor's practice of offsetting full value differences for different tax years is improper. The assessor should process escape assessments or assessment reductions for each year for which these changes are discovered, and leave the offsetting of tax differences to the county auditor.

NOTIFICATION OF THE COUNTY AUDITOR

The process described in statute for adjusting a property tax liability requires that an assessor initiate a roll change for a difference discovered during an audit. The taxpayer is then billed for the additional taxes for an under-assessment, but must file a claim for refund for the tax refund involving over-assessments. Revenue and Taxation Code section 533 requires that when assessment roll changes are made as a result of an audit, "...the tax refunds resulting from the incorrect assessments shall be an offset against proposed tax liabilities, including accumulated penalties and interest, resulting from escaped assessments for any tax year covered by the audit." To properly implement section 533, the assessor must advise the county auditor of proposed escape assessments as well as roll changes resulting from correction of an over-assessment.

The Fresno County Assessor's present, illegal practice of netting the assessment changes from different years circumvents the statutory requirement that the taxpayer file a claim for refund for excess tax resulting from an over-assessment. Also, if the auditor is not aware of proposed tax liabilities, it is possible for a taxpayer to obtain a refund check from a prior year's assessment roll change while contemplated tax liabilities for other years are being processed. We recommend that the assessor notify the county auditor of proposed escape assessments and over-assessments for which Revenue and Taxation Code section 533 requires an offset.

AUDIT FOR ALL YEARS OPEN UNDER THE STATUTE OF LIMITATIONS

In our last survey report, we recommended that audits be expanded to cover all years open under the statute of limitations when a discrepancy or irregularity is found in the year selected for

audit. The assessor has not implemented this recommendation, except for *some* audits of taxpayers that consistently fail to file a property statement.

When an audit of a “non-mandatory fail to file” account reveals an over-assessment, only that one year is reviewed and an assessment change is made. A “cursory review” of prior years is performed to ensure that no escape assessments exist. The notation is made on the audit report that prior years were not audited per BOE Rule 192 (e). However, when audits for the test year reveal an underassessment, an audit of the four-year period open under the statute of limitation is conducted and escape assessments are made when discovered.

Although BOE Rule 192 applies specifically to mandatory audits, the only difference between mandatory and non-mandatory audits is that once the dollar threshold (\$300,000) is reached, the mandatory accounts must be audited once in four years. Both types of accounts are subject to the same rules and standards of audit and assessment procedures.

The assessor’s policy of expanding audits for escape assessment situations, but limiting audits to one year for refund situations, is not an acceptable assessment policy; it does not promote equitable or accurate assessment. We recommend the assessor require all audits be expanded to all years open under the statute of limitations, unless the test year results in no change in assessment.

Property Statements

Fresno County annually processes property statements for 21,087 businesses, 14,494 agricultural properties, 685 aircraft (including 12 certificated aircraft), and 11,457 boats. Revenue and Taxation Code section 443.1 requires that whenever any taxpayer files a property statement, timely and in duplicate, with a request that the assessor mark on the statement, opposite each category of property reported on the statement, the full value of such category of property as determined by the assessor, the assessor shall perform such service and shall return the duplicate to the person filing it no later than July 15 of the year in which it was filed.

RECOMMENDATION 12: Comply with Revenue and Taxation Code section 443.1 by always returning duplicate property statements.

The assessor routinely requires a self-addressed postage paid envelope before returning a duplicate filing. The assessor has no authority to require taxpayers to provide self-addressed postage paid envelopes in order to receive this service. We recommend the assessor comply with section 443.1, and return timely filed duplicate property statements without exception.

Valuation

The usual practice for the valuation of business personal property is to adjust acquisition costs for changes in price level and accrued obsolescence. The adjustments for price level changes are known as replacement cost new index factors. The adjustments for accrued obsolescence are

known as percent good factors. There are a number of sources for these factors, but most assessors rely primarily on the State Board of Equalization to furnish the factors. Each type of factor is published annually.

RECOMMENDATION 13: Improve business property valuation by: (1) using the equipment index factors as recommended in Assessors' Handbook Section 581; and (2) using the BOE's recommended value factors to value computers.

ASSESSORS' HANDBOOK SECTION 581

The BOE annually publishes equipment price index factors that are used to compute replacement costs by trending historical costs for changes in price levels. Assessors' Handbook Section 581 (AH 581), *Equipment Index Factors*, contains 20 index factor categories for commercial, industrial, agricultural, and construction equipment.

As in prior surveys, our review noted that Fresno County continues to use only ten factors. The various categories contained in AH 581 measure the change in equipment prices for enterprises determined by the categories. These changes can vary greatly from one category to another. The assessor's practice of using a smaller number of categories for a broad range of property types results in the averaging of values for the different property types rather than making an accurate estimate of value for each property. The result is a lack of equalization among those businesses that have shown greater or lesser increases in equipment costs than the broader categories used by the assessor.

It should be the goal of all county assessors to provide the most accurate estimates possible of property valuations for assessment purposes. We again make the recommendation that the assessor use all of the equipment index factor categories as recommended in AH581.

COMPUTERS

The valuation of computers and related equipment (herein referred to as computers) has been a contested issue between taxpayers and assessors for the last few years. In its continuing effort to maintain proper, equitable, and uniform property tax assessment, the BOE has recommended factors for assessors to use when valuing computers. For the 1997 lien date, the BOE issued Letter to Assessors (LTA) 97/18, dated April 2, 1997, containing the new valuation factors for the three tables similar to those provided in LTA 96/27. The computer valuation factors are listed in three tables: (1) mainframe computers; (2) mid-range; and (3) personal computers. The tables for personal and mainframe computers represent a recalculation of the depreciation curves that were used to calculate those categories for the 1996 lien date. The table for mid-range computers represents a new curve based on all data accumulated to date. The Board members reviewed all data presented by the BOE's Property Taxes Department staff, the California Assessors' Association, and representatives of the computer industry. The Board members then authorized the publication of the computer valuation tables for the 1997 lien date.

For the 1997 lien date, the assessor used some of the BOE's recommended factors in valuing computers. The assessor's office used three factor tables for the computer categories of personal,

mid-range and mainframe, as recommended by the BOE. However, the assessor's office only used the BOE's recommended factors for the 1992 through 1997 acquisition years. For 1991 and earlier years of acquisition, the assessor's office applied a factor of 10 percent for all categories of computers.

The BOE's recommended factors by computer category, as set forth in LTA 97/18 for acquisition years 1988 through 1991, are as follows: personal (2%, 2%, 4%, 6%), mid-range (2%, 3%, 5%, 8%), and mainframe (2%, 4%, 6%, 9%). Application of a 2% factor is recommended for vintage years earlier than 1988.

The valuation factors recommended by the BOE were developed after extensive data gathering, analysis, and consultation with the computer industry and assessors. We recommend that the assessor assess all computers by applying all the factors contained in the LTA's.

OTHER TAXABLE PERSONAL PROPERTY

Equipment in Licensed Vehicles

Revenue and Taxation Code section 10758 specifies that the license fee imposed on motor vehicles is in lieu of all taxes according to value levied for state or local purposes on vehicles of a type subject to registration under the Vehicle Code, whether or not the vehicles are registered under the Vehicle Code. Thus, any motor vehicle subject to the license fee is not subject to ad valorem property taxation, including equipment installed in licensed vehicles. The fact that additions or modifications to vehicles may not be reported to the Department of Motor Vehicles, and therefore are not reflected in the license fee, does not mean that these additions or modifications are subject to property taxation.

RECOMMENDATION 14: Stop assessing cellular telephones and two-way radios installed in licensed vehicles.

The assessor assesses cellular telephones and two-way-radios installed in licensed vehicles. We believe such equipment becomes a part of the vehicle and is subject to the vehicle license fee and not to the ad valorem property tax. We recommend the assessor stop assessing cellular telephones and two-way-radios installed in licensed vehicles.

Vessels

The assessor's office has an effective discovery program; information on boats is received through reports from the Department of Motor Vehicles (DMV), marinas, taxpayer-filed boat information forms, and reports from other county assessors reporting boats that are relocated from their counties to Fresno County. The assessor has implemented a computerized Boat Control Card System that contains ownership data, the purchase date and price of the boat, the current value, and a description of each boat assessed in the county. The system enables users to access information on boats by California registration number (known as a CF number), assessor's parcel number, or account number. The assessor's staff processed 11,457 boat

property statements which resulted in 6,877 boat assessments with a total value of \$35,124,900 for the 1997 lien date. The assessor exempts all vessels valued at \$1,500 or less.

RECOMMENDATION 15: Improve the boat assessment program by: (1) annually appraising pleasure boats at market value; (2) assessing boats valued over \$400; and (3) using the Board-approved Vessel Property Statement AH 576-D, when a penalty for failure to file the property statement is contemplated.

MARKET VALUE

When a boat is first assessed in Fresno County, the initial assessed value is based on either: (1) the cost code assigned by the DMV, less a 10 percent first year depreciation factor; (2) the purchase price reported to the assessor by the boat owner; (3) the sales price reported to the DMV; or (4) retail selling prices from boat value guide books such as BUC, ABOS and NADA. For subsequent assessments, this initial value is reduced by 10 percent annually, as long as the boat remains in the same ownership, until a value of \$1,500 is reached. At that value level, the boat is no longer assessed.

The 10 percent annual value reduction is an administrative convenience because it takes less time than making market value appraisals. However, the assessor has not done any studies of market depreciation to substantiate the 10 percent depreciation factors applied to all boats. We recommend that the assessor appraise all pleasure boats annually at market value by using boat valuation guides, or by developing depreciation factors based on market data.

BOATS VALUED OVER \$400

The assessor exempts vessels with market values of \$1,500 or less. Revenue and Taxation Code section 228 requires that a vessel with a market value of \$400 or less be exempt from property taxation. The assessor cannot legally increase this exemption limit unless a low-value resolution raising this limit is in effect in the county. Fresno County does not have such a resolution.

A list of boats valued between \$400 and \$1,500 is not maintained. Therefore, we were unable to determine the exact number of boats that fall between the statutory exemption level of \$400 and the total under \$1,500 that are escaping assessment. For the 1997 lien date, at least 4,488 boats valued at \$1,500 or less were not assessed. Boats valued at \$1,500 or less when first situated in the county are not entered into the computer system, however, ownership data is retained in a Boat Control Card File with a “no value status.” Therefore, the assessor has no inventory of boats in that category.

We recommend the assessor stop allowing boats to escape assessment when the market value is more than \$400 and less than \$1,500.

PRESCRIBED VESSEL FORMS

Revenue and Taxation Code section 441 requires certain taxpayers to file a signed property statement with the assessor. Section 452 instructs the Board to prescribe in detail the content of

property statements. BOE Rule 171 requires property statements to be approved by the Board. Section 463 provides for a 10 percent penalty of the assessed value if the taxpayer fails to file or does not timely file the property statement.

Each year the assessor submits, for Board approval, copies of those property statement forms that will be used in the ensuing year. One of the forms submitted for approval was the prototype of AH 576-D, Vessel Property Statement. However, the vessel property statement form submitted for approval is not the form used by the assessor. The assessor uses a form titled "Boat & Motor Property Statement." The assessor requests information on this form from boat owners who have boats located in Fresno County. The form and accompanying cover letter used by the assessor refer to a 10 percent penalty authorized by Revenue and Taxation Code section 463 for failure to file the statement timely.

This code section specifies a penalty that is to be imposed for a taxpayer's failure to file or late filing of a required property statement. The penalty can be applied only if Board prescribed forms are used. The assessor's boat and motor property statement form should not be used with the penalty language it contains because it is not a Board approved property statement. We recommend the assessor not apply or refer to the penalty authorized by Revenue and Taxation Code section 463 unless it is in the context of a Board prescribed property statement.

Aircraft

For the 1997 lien date, Fresno County processed 685 aircraft property statements, which resulted in 651 aircraft assessments, including 12 certificated aircraft, with a total assessed value of \$47,061,330. The assessor's staff has an effective program for discovering aircraft situs in the county. They use aircraft listings and reports from the Federal Aviation Administration (FAA), the State Board of Equalization, airport managers, and field canvassing.

The appraiser responsible for appraising aircraft regularly attends the California Assessors' Association Aircraft Subcommittee meetings. The subcommittee recommends values and factors to be used in valuing certificated aircraft. These meetings are a useful source of information and training for the appraisal of such aircraft.

For the 1997 lien date, 12 certificated aircraft were assessed in Fresno County. Revenue and Taxation Code section 1152 and Property Tax Rule 202(c) describe the inter-county allocation formula used for assessing certificated aircraft. The allocation formula consists of: (1) ground time and flight time and (2) aircraft arrivals and departures. These two factors, along with the values for the aircraft, are the basis for each county's assessed values of these aircraft. The appraiser who is responsible for appraising these aircraft determines the aircraft values from the listing of *Recommended Values for Commercial Aircraft*, published by the Aircraft Advisory Subcommittee, and properly allocates the values.

For the 1996 lien date, the assessor implemented a computerized aircraft control card system for general aircraft. This system contains current information such as owner's name and address, current value, prior owner, location of aircraft, manufacturer's name, model name, aircraft serial

number and FAA (tail number) of the aircraft. The system can be accessed by use of a FAA number, an assessor's parcel number, or a business account number.

California assessors are required to annually assess aircraft at market value. Letter to Assessors (LTA) 97/03, dated January 31, 1997, recommends that assessors use the Aircraft Bluebook Price Digest as the primary guide for valuing general aircraft and the Vref Aircraft Value Reference as an alternate for planes not listed in the Aircraft Bluebook Price Digest. LTA 97/03 also directs that listed retail values shall be reduced 10 percent to provide reasonable estimates of fair market values for aircraft in truly average condition on the lien date. The staff appraiser uses a computerized version of the Aircraft Bluebook Price Digest, which is an effective use of time and aids in the proper calculation of adjustments.

The staff appraiser reduces the value guide list price by 10 percent, makes additional appropriate adjustments for aircraft condition such as abnormal engine hours, avionics, major damage, abnormal airframe hours, and adds an increment for sales tax. During field canvassing, the appraiser notes other factors that might affect the aircraft's value.

RECOMMENDATION 16: Improve the aircraft assessment program by: (1) complying with the requirements of Rule 252(a) to list general aircraft values in a separate section of the roll; (2) verifying the 12 days of public display for aircraft granted the exemption for historical significance under section 220.5; and (3) including sales tax in the value of aircraft unless the aircraft qualifies for the sales tax exemption as a "common carrier".

PLACEMENT ON ASSESSMENT ROLL

Revenue and Taxation Code sections 5451, et seq., require that revenue derived from general aircraft assessments be allocated in a different manner than the method used for general property tax revenues. BOE Rule 252(a) (Minimum Contents of "Machine-Prepared" Local Rolls) requires that the assessment roll prepared by the assessor of each county contain, in a separate section of the roll, the assessed value of any personal property for which tax revenues are subject to allocation in a manner different from that provided for general property tax revenues (e.g. general aircraft).

In Fresno County the assessor lists aircraft values on the unsecured roll by assessor's parcel number. Aircraft values are identified, but they are interspersed with other types of assessments. We recommend that the assessor comply with Rule 252(a) and list the assessed values of general aircraft in a separate section of the roll.

HISTORICAL AIRCRAFT EXEMPTION

Revenue and Taxation Code section 220.5 provides that aircraft of historical significance shall be exempt from taxation only if all of the conditions set forth in subdivision (b) of the section are met. One of the conditions is that the aircraft be available for public display at least 12 days during the 12-month period immediately proceeding the lien date for the year for which the exemption is claimed.

For the 1997 lien date, there were 34 aircraft granted the historical aircraft exemption in Fresno County. When a new application for the exemption is received, the appraiser responsible for the valuation of aircraft explains the conditions for exemption to the applicant.

The exemption claim form used by the Fresno County Assessor requires the claimant to list all public displays with the date, number of days, location, and name and telephone number of the display site's owner for the year immediately preceding the lien date. The assessor accepts the claim for exemption without verification of the reported information. The assessor should establish a procedure for verifying the 12 days of public display; we recommend randomly sampling the claims for exemption by verifying display events.

SALES TAX

For property tax purposes, the general rule for determining market value is that, where price is the basis of value, sales tax and freight charges are elements of value (Xerox Corp. v. Orange County 66 Cal.App.3d 746). Accordingly, if the buyer is liable for sales tax, then the value should include sales tax. Aircraft used by "common carriers" are not subject to sales tax, and are valued without sales tax as an element of value because the consumer (the air carrier) is never liable for sales tax on purchases of such equipment; therefore the replacement cost could not include sales tax.

Revenue and Taxation Code section 6366 exempts the sale of an aircraft to any person using the aircraft as common carrier **from sales tax**. BOE Sales Tax Regulation 1593, subdivision (a), defines "common carrier" as any person who engages in the business of transporting persons or property for hire or compensation and who offers the service indiscriminately to the public or to some portion of the public. The aircraft is deemed a common carrier if it is used in common carriage for more than one half its operational use. If leased or acquired after January 1, 1997, the aircraft must annually gross the lesser of 20 percent of the aircraft's purchase price or fifty thousand dollars (\$50,000).

Aircraft used in air taxi service in Fresno County are predominantly in nonscheduled service. The assessor values nonscheduled air taxi aircraft in the same manner as general aviation aircraft, except that sales tax is not included in the value. Aircraft in scheduled air taxi service are valued in the same manner as certificated aircraft and sales tax is not included in the value. The criteria for exemption from sales tax on aircraft sales is whether or not the aircraft is to be used as a common carrier; the distinction of nonscheduled vs. scheduled is not relevant.

We did not find any indication that the assessor is making a determination that the aircraft used in unscheduled air taxi service are "common carriers", as defined by state statute and regulations. Absent such a determination, sales tax should be included in the taxable value of the aircraft. We recommend that sales tax be included in the taxable value of all aircraft unless the aircraft is in common carrier service.

Manufactured Homes

Manufactured homes, unless placed on a permanent foundation as described in Health and Safety Code section 18551, are classified as personal property and are assessed according to the

Manufactured Home Property Tax Law, (Revenue and Taxation Code sections 5800 through 5842). This section of the law applies the principles of article XIII A to the assessment of manufactured homes classified as personal property. Unlike other personal property, manufactured homes: (1) must be assessed on the secured roll; (2) must receive a tax bill payable in two installments; (3) are subject to supplemental assessments (except in the case of voluntary conversions to local property tax); (4) must have a factored base year value; (5) may receive the homeowners' exemption; and (6) qualify as property eligible for base year value transfers.

At the time of our survey, Fresno County assessed approximately 5,600 manufactured homes. Of these, approximately 2,100 are located outside the 100 manufactured home parks. The assessor has assigned two appraisers to value the homes located in manufactured home parks. The appraiser who is assigned to a specific geographic area values all other manufactured homes.

The assessor revised the manufactured home valuation procedures in January 1994. Staff appraisers currently consult the *Kelley Blue Book Official Manufactured Housing Guide*, dealer reported sales prices, and individual manufactured home sales before arriving at an assessed value. Another source consulted is the Assessors' Handbook Section 531.35 (manufactured home unit cost factors, issued by the State Board of Equalization).

The manufactured home assessment records we reviewed were clear, concise and well documented. These properties are tracked through the county's computer system by vehicle identification number (VIN) and assessor's parcel number (APN) which aids in property assessment in the event of removal from one site and relocation to another.

Revenue and Taxation Code section 5813 requires that the taxable value of a manufactured home be the lesser of its base year value, compounded by the annual inflation factor, or its fair market value as determined pursuant to section 5803 of the Revenue and Taxation Code. The assessor has developed a computer program that calculates declining market values each year for all manufactured housing. Four criteria are essential for the operation of the program: (1) base year value; (2) date of the latest transfer; (3) use code the county uses to identify type of transaction; and (4) year built. Sales information is stored in a computer database. The data is then transferred from the main database into the calculation program. The prospective value is calculated for each manufactured home; this is done every year regardless of the vintage of the base year.

During our review, we compared the assessor's values with data from the *Kelley Blue Book Official Manufactured Housing Guide*, and in many cases, found the assessor's values were less than the values indicated by that publication, but not by meaningful amounts. We commend the assessor for a well-organized, well-administered manufactured home assessment program.

Animals

Various sections of the Revenue and Taxation Code exempt most animals from property taxation. Pets are exempt under section 224. Animals as business inventory are exempt under sections 129 and 219; Property Tax Rule 133 extends the inventory exemption to animals used for the management of livestock. Racehorses are exempt from property taxation but are subject

to an annual tax in lieu of the ad valorem property tax; the taxation of racehorses is discussed in the administrative topics section of this survey. Show horses are the main category of animals used in a trade or business that are subject to property taxation. Show horses, and other horses used in a trade or business that are not exempt, are subject to ad valorem taxes in the same manner as other personal property.

SUGGESTION 6: Use the BOE-prescribed version of Form AH 571 F-2.

The Fresno County Assessor does not use the current version of BOE-prescribed Form AH 571 F-2, Supplementary Schedule to the Agricultural Property Statement, Registered and Show Horses Other Than Racehorses. The front side of this form is for reporting purposes; the backside provides reporting instructions.

The assessor uses a modified version of the front-side of this form with the instructions from the BOE's current prescribed version. The instructions do not correspond to the modified form. For example, the instructions refer to columns 3, 4, and 5, as color, sex, and breed, respectively, and columns 3, 4, and 5 on the form are actually sex, breed, and date purchased.

Obviously the instructions should correspond to the reporting form in order to avoid confusing the taxpayer. We suggest that the assessor use the current version of the BOE prescribed Form AH 571 F-2.

ASSESSOR'S
RESPONSE
TO
BOARD'S
RECOMMENDATIONS



William C. Greenwood
Assessor - Recorder

July 23, 1999

RECEIVED

OCT 18 1999

Dick Johnson, Deputy Director
Property Tax Division
State Board of Equalization
P. O. Box 942879
Sacramento, CA 94279-0063

County Property Tax Division
State Board of Equalization

Dear Mr. Johnson:

In accordance with Section 15645 of the California Government Code, the following response to the State Board of Equalization's Assessment Practices Survey of Fresno County is hereby provided.

This response details those areas where we believe improvements are feasible, notes areas of disagreement in proposals, or, in some areas, rejection where the proposal is deemed impractical or unfeasible.

Choices made by this office to accommodate reduced budgets often means some work is done with less proficiency than what would be expected if we were operating with a full staff. While I seriously consider recommendations from the survey team which address matters I can control, I do not have unilateral power over my budget. If resources were available, more and better appraisals could be done, better records management and more efficient work systems could be developed. This office will continue to search for more effective and efficient ways to accomplish our responsibilities and goals.

The constructive criticism offered by the State Board Survey Team appears to be developed under a presumption that local and state budgets will support Assessor projects irrespective of the cost. A review of past budgets would not support that theory.

I would suggest that the purpose and extent of this report should be reviewed to determine if the benefits derived therefrom are in balance with the total cost to the taxpayers of this State.

Yours very truly,

A handwritten signature in cursive script that reads "William C. Greenwood".

William C. Greenwood
Fresno County Assessor-Recorder

WCG:jf

RECOMMENDATION 1: Do not exempt low-value from assessment unless the board of supervisors adopts a current low value exemption resolution.

RESPONSE: We concur. We are preparing a Low Value Resolution for consideration by our Board of Supervisors.

RECOMMENDATION 2: Comply with Revenue and Taxation Code section 533 when identifying escape assessments on the assessment roll.

RESPONSE: We concur. Our installation of a new property tax system will accommodate this recommendation.

RECOMMENDATION 3: Use the date of enrollment as the date escape assessments are added to the roll, not the date an audit is completed.

RESPONSE: We concur. We will indicate on the escaped assessment transmittal that the Auditor-Controller is required to calculate interest to the date of enrollment.

RECOMMENDATION 4: Comply with Revenue and Taxation Code section 75.55(b) by not canceling small supplemental assessments without authorization from the board of supervisors.

RESPONSE: We concur. As section 75.55 resolution will be taken to our Board of Supervisors.

RECOMMENDATION 5: Improve the California Land Conservation Act (CLCA) assessment program by: (1) relating the risk component in the CLCA capitalization rate to water availability and (2) developing written CLCA assessment practices and procedures.

RESPONSE: (1) As stated in the prior assessment practices survey response, we believe risk for the availability of water is correctly reflected by the appraiser in projections of economic rent. As stated in AH 521 "Where an adequate water supply is a concern, the appraiser must account for the uncertainty either in the projected income stream or in the risk component added to the capitalization rate."

(2) It is always good policy to have written procedures for all phases of work within the Assessor's office. As resources become

available, we intend to develop a written summary of CLCA procedures.

RECOMMENDATION 6: Improve the possessory interest (PI) assessment program by: (1) using a reasonably anticipated term of possession; (2) adding the present worth of future contract rents to PI equity selling prices; (3) not discounting PI values for lack of liquidity; (4) increasing documentation of the PI assessment record; and (5) using BOE approved capitalization techniques when valuing PI's.

RESPONSE: We concur.

RECOMMENDATION 7: Improve the assessment procedures for water company properties by: (1) increasing the discovery effort for assessable water company property and (2) using unitary valuation techniques to develop current market values of water company property.

RESPONSE: We concur.

RECOMMENDATION 8: Improve assessment procedures for petroleum properties by: (1) recognizing abandonment expenses the same year as the economic limit of the property; (2) correctly determining the base year value of a property; and (3) revising the letters that request information from owners.

RESPONSE: (1) We believe our method for handling abandonment expenses is a reflection of actual market experience.
(2) Your comments are noted.
(3) We concur.

RECOMMENDATION 9: Appraise mineral properties as a unit.

RESPONSE: We believe our appraisal method does estimate the market value of the taxable property.

RECOMMENDATION 10: Improve the assessments of cable television systems by: (1) including anticipated rate increases in income projections when using a discounted cash flow capitalization technique; (2) auditing the income and expense data supplied by the taxpayer; (3) including pole make-ready costs when valuing the cable distribution system; and (4) assessing supplies being held for inclusion into house-drops.

RESPONSE: (1) We will include your suggested appraisal technique in our reappraisal of cable television systems.
(2) (3) (4) We concur.

RECOMMENDATION 11: Improve the audit program by: (1) not netting multiple years' audit changes; (2) notifying the county auditor of audit findings that could result in offsetting tax refunds and liabilities; and (3) adopting a consistent policy for determination of the years to be audited.

RESPONSE: (1) We concur.
(2) We will give appropriate notice to the Auditor/Controller when offsets are potential.
(3) Our current policy is to audit all open years.

RECOMMENDATION 12: Comply with Revenue and Taxation Code section 443.1 by always returning duplicate property statements.

RESPONSE: We will comply with your interpretation of section 443.1 (R&T).

RECOMMENDATION 13: Improve business property valuation by: (1) using the equipment index factors as recommended in Assessors' Handbook Section 581; and (2) using the BOE's recommended value factors to value computers.

RESPONSE: (1) The categories required for proper reporting on property statements are logical but not precise. We should not automatically assume that using more trend factors will result in a precise determination of market value. We are dealing with booked prices which, when factored and adjusted are, at best, approximations of fair market value. Our new property system should allow an opportunity to see if using all categories and trend factors improves the valuation of taxable property.
(2) We are currently using the recommended SBE computer factors with the exception we have a 10% floor.

RECOMMENDATION 14: Stop assessing cellular telephones and two-way radios installed in licensed vehicles.

RESPONSE: We concur.

RECOMMENDATION 15: Improve the boat assessment program by: (1) annually appraising pleasure boats at market value; (2) assessing boats valued over \$400; and (3) using the Board-approved Vessel Property Statement AH 576-D, when a penalty for failure to file the property statement is contemplated.

RESPONSE: (1) The initial appraisal of all boats is done by an auditor-appraiser. Subsequent assessments allow for an annual depreciation of 10%. We use the BUC Book and the Blue Book as guides for our appraisals. Our values are produced efficiently, effectively and are within an acceptable range.
(2) We will consider your comments in the development of the Low Value Resolution.
(3) We concur.

RECOMMENDATION 16: Improve the aircraft assessment program by: (1) complying with the requirements of Rule 252(a) to list general aircraft values in a separate section of the roll; (2) verifying the 12 days of public display for aircraft granted the exemption for historical significance under section 220.5; and (3) including sales tax in the value of aircraft unless the aircraft qualifies for the sales tax exemption as a "common carrier".

RESPONSE: (1) The development of our new property tax system should resolve this issue.
(2) We will sample (audit) this class of property to determine the accuracy of exemption claims.
(3) We include sales tax in the valuation of aircraft on the current roll.

SUGGESTION 1: Improve the administration of the racehorse tax program by establishing a procedure for documenting compliance with BOE Rule 1054(a)(2).

RESPONSE: We will document our compliance with Rule 1054(a)(2).

SUGGESTION 2: Record all building permits on appraisal records.

RESPONSE: Your suggestion is noted.

SUGGESTION 3: Initiate a program for spot-checking self-reported new construction costs.

RESPONSE: The plan is impeded by resource allocation for resolution of responsibilities of greater priority.

SUGGESTION 4: Improve the assessment program for properties with a taxable value that is less than factored base year value by (1) increasing the documentation that supports the market value estimate and (2) maintaining a current factored base year value for those properties.

RESPONSE: Your suggestion will be considered.

SUGGESTION 5: Improve the assessment procedures for Timber Production Zone (TPZ) properties by inventorying these properties for existing compatible uses and including the value of those uses in the assessment.

RESPONSE: We will request information regarding compatible uses from TPZ landowners.

SUGGESTION 6: Use the BOE-prescribed version of Form AH 571 F-2.

RESPONSE: We concur.